BriAlto

ENERGY CORPORATION

1997 ANNUAL REPORT

BriAlto
ENERGY CORPORATION

CORPORATE PROFILE

BriAlto Energy Corporation is a Calgary-based, junior oil and gas resource company trading on The Alberta Stock Exchange, under the symbol "BTO.A".

Incorporated as a numbered company during 1994, the Company changed its name to BriAlto, altered its capital structure and conducted an initial public offering, using the "A – B flow-through share" structure in late 1996.

BriAlto's multi-disciplined management team has over 55 years of technical experience. The team is focused on building BriAlto into a successful exploration company, correspondingly adding shareholder value through a combination of quality oil and gas prospecting and diligent, inventive deal making. The management team is motivated to maintain lower than industry average finding and development costs and overhead.

The Company's production has grown consistently since operations were initiated in late 1996. BriAlto's "finding" expertise and focus is on light oil production, both from vertical and horizontal wells, in southeastern Saskatchewan. With the foundation provided by its southeastern Saskatchewan production, the Company is expanding its exploration portfolio to include natural gas and higher risk, higher reward prospects.

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ANNUAL AND SPECIAL MEETING

The Annual and Special Meeting of Shareholders will be held at 3:00 p.m. on Thursday, June 18, 1998 in the Cardium Room of The Calgary Petroleum Club, 319 5th Avenue S. W., Calgary, Alberta. All shareholders are encouraged to attend and participate in the business of the meeting. Those unable to attend should complete their Form of Proxy, indicating their preference in the affairs to be conducted and return the Form to CIBC Mellon Trust Company.

Abbreviations

stb	stock tank barrels	boepd	barrels of oil equivalent per day
mstb	thousand stock tank barrels		
bbl	barrel	mcf	thousand cubic feet
bopd	barrels of oil per day	mcfpd	thousand cubic feet per day
boe	barrel of oil equivalent (10 mcf = 1 bbl)	mmcf	million cubic feet
		WTI	West Texas Intermediate

Alan R. Tolg
President and CEO

PRESIDENT'S MESSAGE TO SHAREHOLDERS

1997 was an active and exciting year for BriAlto Energy Corporation. The Company participated in ten successful oil wells and negotiated a series of corporate and/or production acquisitions within our core focus area of south-eastern Saskatchewan.

BriAlto averaged 82 bopd in 1997 and exited the year at 204 bopd. Current production is approximately 225 bopd. In our first full year of operations, the Company generated net earnings of $28,893 ($0.01/share) and cash flow from operations of $297,353 ($0.07/share) on oil and gas revenues of $645,965. At January 1, 1998, proven and probable reserves were 702,585 stb. 1997 finding and on-stream costs were $4.98/bbl. The Company had a field netback of $15.41/bbl on an average wellhead price of $24.07/bbl.

Commodity prices have slipped significantly in the first quarter of 1998. With solid cash flow, low overhead and presently $1.5 million in the bank, BriAlto is well positioned to take advantage of more reasonably priced acquisitions and drilling opportunities. Currently, BriAlto has an inventory of low risk horizontal locations to drill through the balance of 1998, and the Company will continue to add high quality prospects to its inventory. In an effort to take advantage of strong gas prices, BriAlto has secured significant interests in a relatively shallow, full cycle gas play at Thunderchild, Saskatchewan. BriAlto anticipates that up to three gas tests will be drilled on the prospect in 1998. The development of threshold reserves and production at Thunderchild will allow for the construction of a gathering and processing facility.

The management and staff of BriAlto would like to thank all of the shareholders for their valued support and advice throughout 1997. 1998 offers a new set of challenges and I am confident we will continue to grow and prosper through the year.

On Behalf of the Board,

Alan R. Tolg
President
May 6, 1998

HIGHLIGHTS

For the Year Ended December 31	1997	1996*	% Change
Financial ($)			
Revenues	645,965	2,148	29,973
Cash flow from operations	297,353	766	38,719
Cash flow per Class A share	0.07	0.00	-
Net earnings	28,893	409	6,964
Net earnings per Class A share	0.01	0.00	-
Capital expenditures	1,535,284	128,987	1,090
Shareholders' equity	5,393,244	1,996,608	170
Class A shares outstanding	7,195,454	3,007,400	139
Weighted average Class A shares outstanding	3,991,203	413,582	865
Class B shares outstanding	97,504	97,504	-
Operating			
Crude oil			
- daily average *(bopd)*	82	0	-
- exit rate *(bopd)*	204	0	-
- price per barrel	24.07	-	-
Proven reserves *(stb) - Jan. 1, 1998*	362,189	21,000	1,625
Proven and probable reserves *(stb) - Jan. 1, 1998*	702,585	21,000	3,246
Finding and on-stream costs *($/bbl)*			
- proven and probable	4.98	6.14	-19
- proven and 50% probable	6.18	6.14	1
Field netback *($/bbl)*	15.41	-	-
Exploration and Development			
Wells drilled			
- gross	10	1	900
- net	1.56	0.14	1,014
Success rate *(%)*	100	100	-
Land			
- net acres	1,328	45	2,851

* *From October 21, 1996 to December 31, 1996*

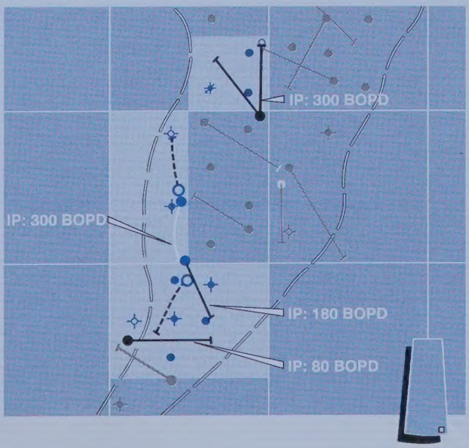
Thom W. Vysohlid, P. Land
Vice President,
Land & Contracts

FOCUS AREA – S.E. & W.C. SASK.

- *MANAGEMENT EXPERTISE*
- *SHALLOW DRILLING*
- *YEAR-ROUND ACCESS*
- *SEISMIC*
- *LIGHT OIL, SWEET GAS*

Ingoldsby

Ingoldsby has developed into a core property for BriAlto. The Company has acquired varied working interests in 1600 gross acres of land and four existing vertical Frobisher oil wells. To date, BriAlto has drilled two dual lateral Frobisher and/or Kisbey horizontal wells and two single lateral Frobisher horizontal wells. Initial production rate for each of the dual lateral horizontal wells was 300 bopd, and for the single lateral horizontal wells was 180 bopd, and 80 bopd, respectively. The Company's net production for this area is 125 bopd, with net reserves of 360.7 mstb (proved plus probable).



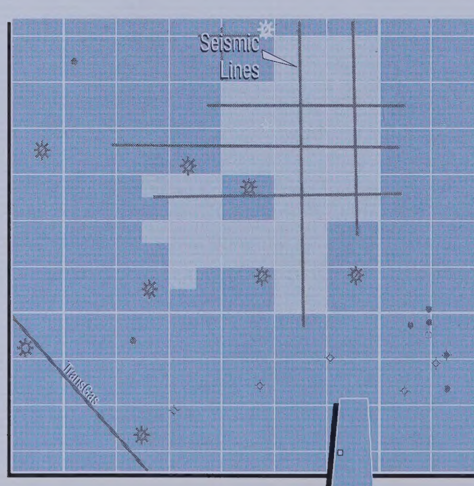
In 1998, BriAlto has plans to drill one additional dual lateral Frobisher/Kisbey horizontal well with a working interest of 28% and a single lateral Frobisher horizontal well with a working interest of 14%. Both of these wells are low risk, infill development locations. In addition, management is looking to increase the Company's production and land inventory in this area through strategic acquisitions and third party joint ventures.

Weir Hill

At Weir Hill, BriAlto acquired an average 36.5% working interest in 880 gross acres of land, two vertical Halbrite zone oil wells and production facilities. In 1997, BriAlto recompleted the two existing vertical wells and increased production from 10 bopd to 28 bopd. Additionally, approximately 20 km. of 2D seismic data was acquired and interpreted on or adjacent to the Company's lands. In 1998, the Company plans to drill at least one Halbrite horizontal well to further exploit the existing reservoir and one vertical Halbrite well to test a seismically defined feature adjacent to the known pool.

Thunderchild

Thunderchild is a shallow Upper Mannville gas prospect located in northwest Saskatchewan. The Company secured a 30% working interest in 10,080 gross contiguous acres immediately northeast of the TransGas regional transportation pipeline. A 65km seismic program was shot over the lands resulting in a number of Colony, McLaren and Waseca bright spot anomalies being identified. In 1998, the Company plans to drill at least three wells to test the best anomalies.



Offsetting the Company's lands are a number of shut-in gas wells together with a large amount of open and expiring Crown land. Management will be diligently pursuing additional lands and reserve acquisition opportunities on the prospect in anticipation of this becoming a core gas area for the Company.

Brian D. Korney, C.A.
Vice President,
Finance, CFO and
Secretary

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion and analysis is a review of the financial and operating results of BriAlto Energy Corporation for 1997 and should be read in conjunction with the audited financial statements and related notes starting on page 10 of this annual report. The Company initiated activity during the last calendar quarter of 1996 with a series of financings, both private and public. BriAlto drilled its first well during December, 1996.

Production

For fiscal 1997, BriAlto averaged 82 bopd. The Company exited 1997 at 204 bopd and current production is approximately 225 bopd. The Company has immaterial gas production at this time.

	1 Q ended March 31	2 Q ended June 30	3 Q ended September 30	Year ended December 31
Average	22 bopd	47 bopd	59 bopd	82 bopd
Exit	62 bopd	60 bopd	100 bopd	204 bopd

Revenue

Petroleum sales for the year were $721,061. The yearly average price received for our oil, which is designated Light Sour Blend (Cromer) and has an approximate 28 degree API gravity, was $24.07 per barrel. During 1997, the benchmark price index of our industry "WTI" decreased from $25.93 U.S. on January 1, 1997 to $17.68 U. S. on December 31, 1997 (a 32% decrease). A parallel decrease was realized in the average price per barrel received by BriAlto. During the first quarter the price was $31.07, the six months ended June 30, 1997 – $24.65 and the nine months ended September 30, 1997 – $24.35. The translation from WTI to the price received by the Company was somewhat mitigated by the performance of the Canadian dollar vis a vis the U. S. dollar.

Royalties

Total royalties paid to the Crown, freehold owners and third parties aggregated $118,708, or $3.96/bbl. Due to Crown royalty-free periods on "new" production in the province of Saskatchewan, the majority of royalties (61%) were paid to freeholders and third parties. As a percentage of petroleum sales, royalties amounted to 16.5%.

Operating Expenses and Field Netback

Lease operating expenses or "lifting costs" were $140,625, or $4.70/bbl. A component of this category is freehold mineral tax, a burden paid by the producer, to the provincial Crown, on petroleum extracted from freehold property. Freehold mineral tax was $0.54/bbl. As a percentage of petroleum sales, lifting costs aggregated 19.5%.

Field Netback (per bbl)

	1 Q ended March 31	2 Q ended June 30	3 Q ended September 30	Year ended December 31
Average	22 bopd	47 bopd	59 bopd	82 bopd
Petroleum sales	$31.07	$24.65	$24.35	$24.07
Royalties and freehold mineral tax	3.91	7.18	4.78	4.50
Operating expenses	3.02	3.26	3.51	4.16
Wellhead netback	$24.14	$14.21	$16.06	$15.41

Depletion and Depreciation Expenses

BriAlto's depletion, depreciation and amortization expenses for 1997 totaled $190,776, or $6.36/bbl. The components were: petroleum depletion and depreciation - $175,461, or $5.86/bbl; a provision for site restoration and abandonment of wells and facilities - $10,258, or $0.34/bbl and depreciation of office equipment - $5,057, or $0.16/bbl.

The Company's year-end ceiling test ensures that capitalized costs do not exceed the after-tax estimated value of future net revenue less certain indirect costs associated with such production. The ceiling test is based on constant prices at December 31, 1997. No write-down of capital costs was required as a consequence of this test. The year-end price used was $22.08/bbl.

General and Administrative Expenses

General and administrative expenses for the year were $207,987 or $6.94/bbl. Expenditures of $88,419 were capitalized to the full cost petroleum and natural gas property pool. As BriAlto's production rate increases, general and administrative expenses will increase; however, on a per barrel basis, this burden will decrease.

Income Taxes

BriAlto had no current income tax liability for 1997. This was due to the tax pools acquired as a result of the purchase of Rosebank Resources Ltd. and to tax pools generated from capital expenditures on oil and gas properties that were in excess of the Company's flow-through share tax deduction renunciation liability to its Class B shareholders.

Deferred income taxes of $77,684, or $2.60/bbl, were recorded during the year. Income taxes would be currently payable except that the Company has tax pools that are superior to the accounting deductions availabe.

BriAlto has approximately $1.5 million of available tax pools. This balance, together with future capital programs, should prevent the Company from incurring the burden of current tax for 1998.

Net Earnings and Funds Provided by Operations

Net earnings for the period were $28,893 or $0.01 per fully diluted share. Funds provided by operations amounted to $297,353 or $0.06 per fully diluted share.

Items affecting Net Earnings and Funds Provided by Operations

	$/bbl	**% of Sales**
Petroleum sales	24.07	100
Royalties and freehold mineral tax	4.50	19
Operating expenses	4.16	17
Wellhead netback	**15.41**	**64**
Interest income	1.46	6
General and administrative expenses	6.94	29
Funds provided by operations	**9.93**	**41**
Depletion, depreciation and amortization	6.36	26
Deferred income taxes	2.60	11
Net earnings	**0.97**	**4**

Capital Expenditures

Additions to petroleum and natural gas properties totaled $1,535,284. BriAlto acquired all of the outstanding shares of Rosebank Resources Ltd. for a deemed

Dana Rode
Executive Assistant

value of $572,808. The purchase price was composed of 250,000 Class A shares, valued at $1.00 per share plus cash. BriAlto completed an amalgamation with Adobe Resources Ltd., prior to year-end, which added the oil and gas properties of that company to BriAlto's balance sheet at an ascribed value of $1,331,061, net of the provision for site restoration.

Additions

	$
Land	149,955
Geological and geophysical	18,473
Drilling and completions	1,140,373
Facilities and equipment	186,317
Other	40,166
	1,535,284

During the year, expenditures in the amount of $975,040 were incurred that related to the flow-through Class B shares issued in December, 1996. The related income tax effect of these expenditures, valued at $434,868, has been deducted from both petroleum and natural gas properties and share capital.

Liquidity and Capital Resources

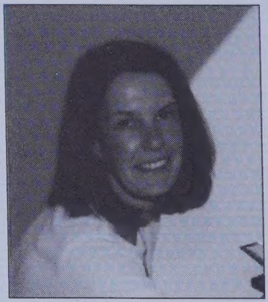
During 1997, BriAlto strengthened its balance sheet by raising equity through two public offerings. The first offering, which closed March 27, 1997 distributed 700,000 Class A shares at $0.75 to the public, transferring $525,000, before offering expenses, to corporate treasury. The second instrument closed on December 30, 1997, raised $1,375,000, prior to offering expenses, and resulted in the issue of 1,100,000 flow-through Class A shares at $1.25 per share. These funds were used to finance the Company's capital expenditure and acquisition program and to increase working capital. At December 31, 1997, BriAlto had a working capital balance of $2,450,748.

The Company has budgeted $3.25 million for capital expenditures, including potential acquisitions, in 1998 (subject to regular review) which will be funded by cash flow, working capital and bank debt. Anticipated bank debt will be less than one time 1997 forecast cash flow. At year-end, BriAlto had a combination of share purchase warrants and share purchase options outstanding equating to 691,240 Class A shares, which, upon exercise, has the potential to bring $606,540 into corporate treasury in the future.

Business Risks

The oil and gas industry is subject to risks not only in the finding and developing of petroleum and natural gas reserves, but also with respect to commodity prices, interest rates, currency translation and environmental concerns. BriAlto attempts to mitigate these risks by:

- focusing on activities and areas in which it has proven expertise;
- developing and exploring prospects in close proximity to its core areas;
- owning production and processing facilities wherever possible to control operating burdens and the amount and timing of additional capital expenditures; and
- maintaining a corporate environmental policy.



Joan Marzetti
Accounting
Consultant

Sensitivities – 1998 Projections

Change in:	Cash flow ($000's)	Per share ($)
Oil price ($1.00 Cdn/bbl)	46	.01
Exchange rate ($0.01 in US/Cdn translation)	2	—

Year 2000

The Company is aware of the issues associated with the programming code in existing computer systems as the millenium (year 2000) approaches. The "year 2000" problem is pervasive and complex as virtually every computer operation will be affected in some way by the rollover of the two digit year value to 00.

BriAlto has received confirmation from its computer software supplier that the data processing system in use will be year 2000 compliant across its entire suite of applications prior to the close of calendar 1998.

Outlook

BriAlto's financial performance is significantly affected by commodity prices, a factor over which the Company has no control. Management believes that oil prices will continue to be volatile during 1998, as prices are impacted by international political events, pricing cartels and other situations beyond fundamental supply and demand economics. In its budgeting process for the future year, BriAlto has assumed an oil price based upon WTI at $15.00 US.

In the future, as the corporate production rate increases, BriAlto intends to hedge its exposure to oil pricing. No more than 50% of our anticipated production volume will be hedged. Hedging decisions will be based upon historical trading ranges and comparison to budgeted levels.

Management is confident that 1998 will be another year of real growth in terms of financial and operating results from ongoing exploration and development activities. BriAlto will continue to pursue acquisition and business combination opportunities, which will expand our exploration and development program and add corporate value.

MANAGEMENT'S REPORT TO THE SHAREHOLDERS OF BRIALTO ENERGY CORPORATION

The accompanying financial statements and all other information presented in this annual report are the responsibility of the Company's management.

The financial statements have been prepared by management in accordance with accounting principles generally accepted in Canada. The Company's internal controls have been designed and maintained by management to provide reasonable assurance that assets are properly safeguarded and that the financial records are sufficiently well maintained to provide relevant, timely and reliable information to management and to allow preparation of the financial statements in accordance with the Company's accounting policies. Where necessary, certain estimates are made by management. The financial statements have been prepared with reasonable limits of materiality and within the framework of the significant accounting policies as summarized in the notes to the financial statements.

KPMG, an independent firm of chartered accountants, has been appointed by the Shareholders to examine the financial statements and to report to the Shareholders. The Audit Committee, consisting of directors, a majority of whom are not employees of the Company, has reviewed the financial statements, including the notes thereto, with management and KPMG. The financial statements have been approved by the Board of Directors on the recommendation of the Audit Committee.

Alan R. Tolg
President and CEO

Brian D. Korney
Vice President, Finance,
CFO and Secretary

AUDITORS' REPORT

To the Shareholders
BriAlto Energy Corporation

We have audited the balance sheets of BriAlto Energy Corporation as at December 31, 1997 and 1996, and the statements of earnings and retained earnings and changes in financial position for the year ended December 31, 1997 and the period from October 21, 1996 to December 31, 1996. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 1997 and 1996, and the results of its operations and the changes in its financial position for the year ended December 31, 1997 and the period from October 21, 1996 to December 31, 1996 in accordance with generally accepted accounting principles.

KPMG

Chartered Accountants

Calgary, Canada
May 6, 1998

BALANCE SHEETS

December 31, 1997 and 1996

	1997	1996
Assets		
Current assets:		
Cash and term deposits	$ 2,238,748	$ 1,963,321
Accounts receivable:		
Production revenues	261,813	—
Cash calls	190,691	—
Joint venture and G.S.T.	126,778	1,036
	579,282	1,036
	2,818,030	1,964,357
Petroleum and natural gas properties (note 3)	2,988,450	128,987
	$ 5,806,480	$ 2,093,344
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities:		
Trade payables	$ 305,702	$ 96,379
Joint venture	61,580	—
	367,282	96,379
Deferred taxes	—	357
Future site restoration	45,954	—
Shareholders' equity:		
Share capital (note 5)	5,363,942	1,996,199
Retained earnings	29,302	409
	5,393,244	1,996,608
Subsequent event (note 7)		
	$ 5,806,480	$ 2,093,344

See accompanying notes to financial statements.

On behalf of the Board:

____________________, Director

____________________, Director

STATEMENTS OF EARNINGS AND RETAINED EARNINGS

December 31, 1997 and period from October 21, 1996 to December 31, 1996

	1997	1996
Revenue:		
Petroleum sales, net	$ 602,353	$ 35
Interest	43,612	2,113
	645,965	2,148
Expenses:		
Operating	140,625	312
Depletion, depreciation and amortization	190,776	—
General and administrative	207,987	1,070
	539,388	1,382
Earnings before income taxes	106,577	766
Deferred income taxes (note 4)	77,684	357
Net earnings	28,893	409
Retained earnings, beginning of period	409	—
Retained earnings, end of period	$ 29,302	$ 409
Net earnings per common share	$ 0.01	$ 0.00

See accompanying notes to financial statements.

STATEMENTS OF CHANGES IN FINANCIAL POSITION

December 31, 1997 and period from October 21, 1996 to December 31, 1996

	1997	1996
Cash provided by (used in):		
Operations:		
Net earnings	$ 28,893	$ 409
Add items not requiring an outlayof cash:		
Depletion, depreciation and amortization	190,776	—
Deferred income taxes	77,684	357
Funds provided by operations	297,353	766
Changes in non-cash working capital	(204,635)	95,343
	92,718	96,109
Financing:		
Share capital issued, net of expenses	3,724,570	1,996,199
Investments:		
Additions to petroleum and natural gas properties	(1,535,284)	(128,987)
Business combination with Rosebank Resource Ltd.	(572,808)	—
Business combination with Adobe Resources Ltd.	(1,433,769)	—
	(3,541,861)	(128,987)
Increase in cash and term deposits	275,427	1,963,321
Cash and term deposits, beginning of period	1,963,321	—
Cash and term deposits, end of period	$ 2,238,748	$ 1,963,321
Funds provided by operations per common share		
Basic	0.07	0.00
Fully diluted	0.06	0.00

See accompanying notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

1. Significant accounting policies:

(a) Petroleum and natural gas properties:

The Corporation follows the full cost method of accounting for petroleum and natural gas expenditures. Capitalized costs include land acquisition, geological and geophysical expenses, lease rentals, and costs of drilling both productive and non-productive wells. Capitalized costs, including production equipment, are depleted by the unit-of-production method based on the Corporation's share of estimated proven reserves, before royalties, of petroleum and natural gas as determined by independent reservoir engineers, with products being converted to a common unit of measure based on equivalent units of energy on a 6:1 basis.

Petroleum and natural gas properties are subject to a ceiling test, under which their carrying value is limited to the future net revenues from production of estimated proven reserves, based on year end prices, plus the unimpaired costs of undeveloped lands, less estimated future general and administrative costs, interest expense, income taxes, and site restoration and abandonment costs. Proceeds of property sales are normally credited to the net book value of oil and natural gas properties without recognizing any gain or loss on disposition unless such a sale would significantly alter the rate of depletion and depreciation.

(b) Other capital assets and related amortization:

The Corporation provides for amortization on other capital assets using the declining balance method at an annual rate of 20%.

(c) Flow-through shares:

The resource expenditure deductions for income tax purposes are renounced to investors in accordance with income tax legislation. Petroleum and natural gas properties and share capital are reduced by the estimated value of the renounced tax deductions when the expenditures are incurred.

(d) Joint operations:

Substantially all of the Corporation's exploration and production activities are conducted jointly with others. These financial statements reflect only the Corporation's proportionate interest in such activities.

(e) Site restoration costs:

Estimated site restoration costs, net of expected recoveries, are provided for over the life of the proven reserves on a unit-of-production basis. Costs are estimated each year by management in consultation with the Corporation's engineers based on current regulations, costs, technology and industry standards. Site restoration expenditures are charged to the accumulated provision account as incurred.

1. Significant accounting policies (continued):

(f) Income taxes:

The Corporation follows the tax allocation method of accounting for corporate income taxes. Deferred taxes are provided to the extent that current taxes have been reduced by claiming amounts, primarily exploration and development costs and capital cost allowance, in excess of the related depletion and amortization recorded in the financial statements.

(g) Earnings per share:

Per share information is calculated on the basis of the weighted average number of Class A shares and Class B shares, assuming a conversion of 10:1, outstanding during the period.

(h) Measurement uncertainty:

The amounts recorded for depletion, depreciation and amortization of petroleum and natural gas properties and the provision for future site restoration costs are based on estimates. The ceiling test calculation is based on such factors as estimates of proved reserves, production rates, oil and natural gas prices and future costs. By their nature, these estimates are subject to measurement uncertainty and may impact the financial statements of future periods.

2. Incorporation and amalgamation:

(a) On May 8, 1997, the Corporation executed an Agreement with the former shareholders of Rosebank Resources Ltd. ("Rosebank"), a Company with a common director of the Corporation, under which the Corporation issued 250,000 Class A shares and cash for all of the outstanding shares of Rosebank.

The effective date of the acquisition was March 1, 1997. The business combination has been accounted for as a purchase of Rosebank by the Corporation with the results of Rosebank operations included in the financial statements from March 1, 1997. Details of the acquisition are as follows:

Petroleum and natural gas properties	$572,808
Consideration given:	
250,000 Class A shares	250,000
Cash	311,434
Combination expense	11,374
	$572,808

2. Incorporation and amalgamation (continued):

(b) On November 25, 1997, the Corporation entered into an Agreement with the former shareholders of Adobe Resources Ltd., under which BriAlto issued one common share for every five Adobe shares.

The effective date of the acquisition is December 31, 1997. The business combination has been accounted for as a purchase of Adobe by the Corporation with the results of Adobe included in the financial statements from December 31, 1997. Details on the acquisition are as follows:

Fair value of net assets acquired:	
Cash	$425,718
Non-cash working capital	102,708
Petroleum and natural gas properties	1,366,757
Provision for site restoration	(35,696)
	1,859,487
Consideration given:	
2,113,054 Class A shares	$1,859,487

3. Petroleum and natural gas properties:

	1997			1996
	Cost	Accumulated depletion and depreciation	Net book value	Net book value
Petroleum and natural gas properties	$3,128,802	$175,461	$2,953,341	$128,987
Other capital assets	40,166	5,057	35,109	—
	$3,168,968	$180,518	$2,988,450	$128,987

During the year ended December 31, 1997 the Corporation capitalized $88,419 (1996 - $nil) of consulting and overhead costs directly related to acquisition, exploration and development activities.

Certain petroleum and natural gas properties having a net book value of approximately $1,400,000 for accounting purposes have nil costs for income tax purposes. These differences arose as a result of business acquisitions and the issuance of flow-through shares.

4. Income taxes:

The provision for income taxes in the statement of earnings reflect an effective income tax rate which differs from Federal and Provincial statutory tax rates. The main differences are as follows:

	1997	1996
Earnings before income taxes	$ 106,577	$ 766
Corporate income tax rate	44.6%	44.6%
Computed income tax provision	$ 47,533	$ 357
Increase (decrease) resulting from:		
Non-deductible crown charges	27,875	—
Non-tax base assets	35,354	—
Resource allowance	(33,078)	—
	$ 77,684	$ 357

5. Share capital:

(a) Authorized:

Unlimited number of voting Class A shares

Unlimited number of voting Class B shares, convertible (at the option of the Corporation) at any time after January 1, 2002 and before January 1, 2004, into Class A shares. The fraction of a Class A share obtained upon conversion of each Class B is calculated by dividing $10 by the greater of $1 and the then current market price of Class A shares. If conversion has not occurred by the close of business on January 1, 2004, the Class B shares will be deemed to be converted to Class A shares effective January 1, 2004.

Unlimited number of Class C preferred shares, issuable in series, the terms of which are fixed by the directors of the Corporation, from time to time.

(b) Issued:

	Number of Shares	Amount
Class A shares:		
Balance, beginning of period	—	$ —
For cash as initial private capital	1,325,000	265,000
Private placement dated November 14, 1996	1,200,000	750,000
Public Offering closed December 31, 1996	332,400	132,960
Founders' Warrants exercised December 31, 1996	150,000	30,000
Share issue expenses	—	(156,801)
Balance, December 31, 1996	3,007,400	1,021,159
Founders' warrants exercised February 5, 1997	25,000	5,000
Public Offering closed March 27, 1997	700,000	525,000
Issued for Rosebank Resources Ltd.	250,000	250,000
Public Offering closed December 30, 1997	1,100,000	1,375,000
Issued upon amalgamation with Adobe Resources Ltd.	2,113,054	1,859,487
Share issue expenses, net of tax effect of $78,041	—	(211,876)
Balance, December 31, 1997	7,195,454	4,823,770

5. Share capital (continued):

	Number of Shares	Amount
Class B shares:		
Balance, beginning of period	—	—
Public Offering closed December 31, 1996	97,504	975,040
Balance, December 31, 1996	97,504	975,040
Effect of tax deductions renounced on flow-through shares	—	(434,868)
Balance, December 31, 1997	—	540,172
Share capital		$ 5,363,942

(c) Flow-through shares:

On December 31, 1996 the Corporation issued 97,504 Class B flow-through shares at a price of $10 per share. As a result, the Corporation subsequently renounced $975,040 of resource deductions for income tax purposes related to certain exploration expenditures.

On December 30, 1997 the Corporation issued 1,100,000 Class A flow-through shares at a price of $1.25 per share. The Corporation has obligations to spend qualifying expenditures of $1,375,000 by December 31, 1998.

(d) As at December 31, 1997, 33,240 (1996 - 33,240) broker warrants were issued in conjunction with the initial public offering, closed December 31, 1996, exercisable at $1.00 per share until June 30, 1998 and 70,000 broker warrants were issued in conjunction with the public offering, closed March 27, 1997, exercisable at $0.75 per share until April 24, 1999. There also exist 48,000 broker options issued with the Adobe acquisition , exercisable at $1.25 until November 28, 1998, and 110,000 broker warrants, exercisable for $1.25 until June 16, 1999.

(e) As at December 31, 1997, 250,000 Class A shares of the Corporation were reserved for issuance to directors, officers and employees, pursuant to options granted, under the Corporation's stock option plan. Each option is exercisable at a price of $0.60 to $0.80 per share on or before October 21, 2001 and July 17, 2002, respectively.

(f) As at December 31, 1997, 180,000 Class A shares were reserved for the exercise of Adobe stock options.

6. Fair values:

The fair values of the Corporation's monetary assets and liabilities approximate their carrying values at December 31, 1997.

7. Subsequent event:

At December 31, 1997, the Corporation passed the ceiling test using the actual commodity prices at year end. Subsequent to year end, crude oil prices have fluctuated and are significantly lower than at December 1997. Based on the Corporation's estimated average oil prices in the first quarter of 1998 of $18.63 per barrel of oil, the carrying value of the Corporation's assets exceeds the estimated future net realizable value by approximately $600,000. Management does not consider the measurement date price to be representative for purposes of estimating future net revenue, as prices are expected to continue to fluctuate, and that no permanent impairment of the value of the Corporation's assets has occurred.

CORPORATE INFORMATION

Directors

Ronald J. Cargo
Chairman and CEO
Bridgetown Energy Corporation
Calgary, Alberta

Kenneth R. Havard
President and CEO
Firefly Resources Ltd.
Calgary, Alberta

William D. B. Koenig
Vice President
Denro Fund Management Alberta Inc.
Calgary, Alberta

Anthony D. Convey
President
Jettstar Resource Services Inc.
Calgary, Alberta

Andrew S. Burgess
Vice President and CFO
Huntington Resources Limited
Calgary, Alberta

Alan R. Tolg
President and CEO
Calgary, Alberta

Brian D. Korney
Vice President, Finance,
CFO and Secretary
Calgary, Alberta

Thom W. Vysohlid
Vice President, Land & Contracts
Calgary, Alberta

Officers

Alan R. Tolg
President and CEO

Brian D. Korney
Vice President, Finance, CFO and Secretary

Thom W. Vysohlid
Vice President, Land & Contracts

Sean J. Korney
Assistant Secretary

Solicitors

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National Bank of Canada
407 - 8th Avenue S.W.
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Auditors

KPMG
Chartered Accountants
1200, 205 - 5th Avenue S.W.
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Evaluation Engineers

Reliance Engineering Group Ltd.
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Registrar and Transfer Agent

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Stock Listing

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Executive Office

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